No. 10,886

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

FEDERAL FARM MORTGAGE CORPORATION
(a corporation),
Appellant,

vs.

HENRY ANDREW PAULSEN,
Appellee.

BRIEF FOR APPELLEE.

WITHERS AND EDWARDS,
153 North Virginia Street, Reno, Nevada,
Attorneys for Appellee.

PERNAU-WALSH PRINTING CO., SAN FRANCISCO

Subject Index

	Page
Issues Involved	6
Argument	7
(a) The Bankruptcy Act	7
Three Year Moratorium Is Not Redemption Statute	17
Conclusions	19

Table of Authorities Cited

Cases

	Pages
Anderson, In re, 23 Fed. Supp. 857	16
Carter, In re, 56 Fed. Supp. 385	18
Corey v. Blake, 136 F. (2d) 162	18
Hard v. Kirkpatrick, 91 F. (2d) 875	18
Home Building and Loan Association v. Blaisdell, 290 U. S. 398, 54 S. Ct. 231	18
Miller, In re, 48 Fed. Supp. 13	8, 9, 11, 19, 20
Stratton v. New, 51 S. Ct. 465	18
Wright v. Union Central Life Insurance Company, 311 U. S. 273, 61 S. Ct. 196, 85 L. Ed. 184	12, 19, 20
Wright v. Vinton Branch of Mountain Trust Bank, 300 U. S. 440, 462, 112 A.L.R. 1455, 57 S. Ct. 556	11

Statutes

Bankruptcy Act:	
Section 75 (n)	8
Section 75 (s)	7
Section 75 (s) (2)	7
Section 75 (s) (3)	7, 10, 15, 18, 20

Congressional Record

Cong. Record	8

No. 10,886

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

FEDERAL FARM MORTGAGE CORPORATION
(a corporation),
Appellant,

vs.

HENRY ANDREW PAULSEN,
Appellee.

BRIEF FOR APPELLEE.

Appellee finds no fault with the "Statement of the Case" in appellant's brief, which is actually nothing but a chronological statement of the various legal steps taken in this proceeding. However, in addition thereto, the appellee feels that the following facts are of importance to show the good faith of the respective parties herein:

1. The appellant was the only creditor objecting to the offer of the appellee, and as a result of its petition prevented the appellee from effecting a compromise with his creditors. (Tr. 38.)

2. The Conciliation Commissioner found that during said three year stay of proceeding, the appellee paid into Court annual rental in the sum of five hun-

dred fifty dollars ($550.00), pursuant to the order staying proceedings, and fully complied with said order. (Tr. 39.) The Conciliation Commissioner also stated in a letter written to Mr. Percy A. Smith, attorney for appellant (Tr. 31-d):

> "I am very much surprised to receive these papers. Mr. Paulsen has paid all the rent that he was required to pay and I have been informed that he is ready to pay in the balance due on the appraised value of the property. The situation seems to be one similar to the discussed 'In Re: Anderson, Fed. Supplement, Vol. 23, 854,' where the Court recognizes that you have a legal right to the procedure now requested by you. In particular the Court says:
>
> " 'Pursuing this undoubted right, the secured creditor may deprive the farmer of the intended ultimate benefit of the provisions of the Act which is the saving of his farm. Yet I think it was in the mind of Congress that the ordinary secured creditor would usually be willing to accept, in lieu of its security, its fair cash value as established by a fair appraisal; that the farmer to refinance himself within the meaning of the Act should be compelled to refinance not his full indebtedness but only the appraised value of the encumbered property as well as the unencumbered property retained by him; that he should not be compelled, in any case, to refinance the entire secured indebtedness, if such indebtedness exceeds the value of its security except to the extent that he might have other property or assets available for that purpose. Otherwise, judging from observation and experience, section 75, subsection

(s), intended to meet a great financial crisis among the farmers, can be helpful in comparatively few cases.'

"My observation in this case is that Mr. Paulsen has acted in good faith during the entire period of the moratorium."

3. That during the three year period, the appellant apparently accepted the original appraisal and permitted the appellee to work under the impression that this appraisal was acceptable to it. That relying on such impression, created by the failure of appellant to demand a reappraisal, the appellee, prior to the expiration of said period and on March 24, 1943, through his attorneys, informed the appellant that he had refinanced himself and could pay the entire balance due into Court. (See letter dated March 24, 1943, Tr. 28.)

4. That prior to replying to this letter, the appellant filed its petition of March 29, 1943 (Tr. 20) praying for the appointment of trustee to sell and dispose of appellee's estate. That thereafter various letters passed between the appellee's attorneys and officers or attorneys for the appellant. (Tr. 28 to 31-w.) That these letters clearly show:

1. That the appellee could, by selling certain personal property consisting mostly of hogs, and thus depleting the production of the farm at a time when wartime need demanded full production, pay off the balance due under the original order. (See letter to Percy A. Smith dated April 5, 1943, Tr. 31-a and 31-b.)

2. That appellee had refinanced himself and was ready, willing and able to pay the said balance into Court. (See letter to Percy A. Smith dated April 6, 1943, Tr. 31-c.)

3. That the appellant, throughout the three year period, would have refused to accept such payment (see letter of M. G. Hoffman dated April 9, 1943, Tr. 31-e), thus showing to the appellee that the making of said payment would be merely an idle gesture on his part since it would be refused, and thus showing that throughout the three year period the appellant was willing to have the appellee work long hours in the hope of salvaging his home and farm, with no intention of abiding by the original appraisement but apparently hoping to gain by the enhancement of value to the property resulting from the appellee's desperate efforts to save his home.

4. That the appellee's attorneys informed the appellant that the appellee's wife had recently secured a little inheritance, and stated:

> "As long as you are the only creditor that is not satisfied rather than sacrifice their pigs and take the bad licking that your action will make them take, she is willing to put in her little inheritance if a reasonable deal can be made with you. What amount will you accept in cash to assign your claim?"
>
> (Letter to Federal Land Bank of Berkeley dated April 13, 1943, Tr. 31-i.)

This attempt to effect a compromise was flatly rejected by the appellant. See letter from M. G. Hoffman dated April 17, 1943 (Tr. 31-i) stating:

> "You ask what amount we will accept in cash to assign our claim. We are not permitted to voluntarily scale down our loans, and, therefore, could not accept a payment from the bankrupt in any amount less than the total amount due."

5. That thereafter appellee requested appellant, as a matter of good faith and as a part of the war effort in order to keep up production, to consent to a reappraisal, with the agreement that the reappraised value would be paid to the bank at once and the appellee thus be given a fair opportunity to save his ranch and pigs. (See letter to Federal Land Bank dated April 19, 1943, Tr. 31-l.) This offer was flatly rejected by the appellant. (See letter of Harold R. Kelly dated April 22, 1943, Tr. 31-q.)

6. That said letters (Tr. 28 to 31-w) as a whole show that at no time in said proceeding has the appellant acted in good faith, but that throughout said proceedings the appellant has acted solely with the view of obtaining possession of the ranch property and regardless of the cost or injustice to the appellee, and has relied on technicalities of the law to prevent the appellee from obtaining any benefit of the Frazier-Lemke Act, and thus has tried to profit by the fruits of the appellee's three years of labor.

7. That the appellee's efforts were appreciated and the attitude of the bank decried under wartime conditions by members of the Churchill County USDA

War Board. (See letter from said Board to Withers and Edwards dated April 22, 1943, Tr. 31-u.)

8. That the appellant is now and has been since March 24, 1943, ready, able and willing to:

a. Pay the balance due on the original appraisal.

b. Pay the balance due upon a reappraisal.

c. Effect a reasonable compromise of this matter.

ISSUES INVOLVED.

The referee certified the following issues:

1. If a bankrupt fails to pay the appraised value into Court and fails to request a reappraisal within three years, and a secured creditor requests the appointment of a trustee under the provisions of the last sentence of Section 75 (s) (3), can the bankrupt thereafter secure a reappraisal with the right to redeem under the first proviso under Section 75 (s) (3)?

2. Whether, under the circumstances in this case as set forth by the correspondence attached to the bankrupt's petition for reappraisal, the appellant is estopped to deny that the bankrupt is entitled to a reappraisal of said property.

ARGUMENT.

(a) THE BANKRUPTCY ACT.

It will be noted from appellant's brief that this proceeding is a proceeding under Section 75 (s) of the Bankruptcy Act (11 USCA, Section 203, page 12). The portions of this section of the Bankruptcy Act to be considered in the instant case are:

1. Section (s) (2): "When the conditions set forth in this section have been complied with, the court shall stay all judicial or official proceedings in any court, or under the direction of any official, against the debtor or any of his property, for a period of three years. During such three years the debtor shall be permitted to retain possession of all or any part of his property, in the custody and under the supervision and control of the court, provided he pays a reasonable rental semi-annually for that part of the property of which he retains possession."

2. Section (s) (3): "At the end of three years, or prior thereto, the debtor may pay into court the amount of the appraisal of the property of which he retains possession, including the amount of encumbrances on his exemptions, up to the amount of the appraisal, less the amount paid on principal: Provided, That upon request of any secured or unsecured creditor, or upon request of the debtor, the court shall cause a reappraisal of the debtor's property, or in its discretion set a date for hearing, and after such hearing, fix the value of the property, in accordance with the evidence submitted, and the debtor shall then pay the value so arrived at into court, less payments made on the principal, for distribution to all

> secured and unsecured creditors, as their interests may appear, and thereupon the court shall, by an order, turn over full possession and title of said property, free and clear of encumbrances to the debtor * * * If, however, the debtor at any time fails to comply with the provisions of this section, or with any orders of the court made pursuant to this section, or is unable to refinance himself within three years, the court may order the appointment of a trustee, and order the property sold or otherwise disposed of as provided for in this title."

The appellee bases his claim for relief under the (n), and Section 75 (s) (6). The appellee fails to see how these sections are applicable since the appellee does not contend that the Court is authorized, under the Bankruptcy Act, to grant a moratorium of over three years, and the appellee further admits that if the appellee fails to comply with the order of the Court, that the Court may terminate or shorten the period of moratorium or the stay of proceedings upon proper showing.

The appellee basis his claim for relief under the terms of the Bankruptcy Act upon the sections hereinabove recited by the appellee. The appellant only cites a few cases to support his contentions in the matter. It will be noted that the references to the Congressional Record contained in paragraph (c), page 16, of appellant's brief, is little more than an extract from a portion of the decision in the case of *In re Miller,* 48 Fed. Supp. 13, discussed by appellant in its brief on pages 18 and 19.

The *Miller* case is the only case we have been able to find which in any way substantiates the appellant's contentions. However, we do not believe the *Miller* case applicable to the case at bar for the reason that Judge Neterer, on page 14, states:

> "The bankrupt failed to comply with the stay order as provided by Section 203, sub. s, supra, Tit. 11 U.S.C.A. or at all, and after expiration of the three years, continued default."

Thus the bankrupt at all times during the proceeding had failed to show his good faith, his ability to refinance himself, or to pay the rent required by the Court, or otherwise comply with the Court order granting the three year stay. After the creditor had asked for a foreclosure, the bankrupt filed a petition for reappraisal. Apparently there was a complete absence of good faith on the part of the bankrupt, and his petition for reappraisal was merely an attempt to stall for time when he was already in default, and hence the Court's denying of this petition, which in effect extended the period of moratorium, was proper.

However, in the case at bar, the facts show that the appellee complied in every respect with the order granting the moratorium, and that prior to the expiration of that period, notified the secured creditor that he had refinanced himself and was able to pay the balance due upon the original appraisal, and requested a slight deferment of payment in order to prevent the sale of certain pigs sooner than they were properly developed, which would have caused a grievous loss to the bankrupt as well as being im-

proper under war conditions. (See letter from Churchill County U.S.D.A. War Board dated April 22, 1943, Tr. 31-u.)

The appellant not only refused to grant any extension of time, but also stated that at any time during the proceedings that the appraised value was paid in, it would have refused to accept the same.

In the *Miller* case the bankrupt was unable to refinance himself and hence, under the Bankruptcy Act, Section 75 (s) (3), the Court ordered the appointment of a trustee, whereas in the case at bar, the facts show that the appellee had been able to finance himself during this period. The Court, under the facts existing in the *Miller* case, had no reason to consider that portion of Section 75 (s) (3) of the Bankruptcy Act, reading:

> "*At the end of three years,* or prior thereto, the debtor may pay into court the amount of the appraisal of the property * * *"

The appellee has found no case holding that under this section of the Act the amount of the original appraisal has to be paid actually into Court *prior* to the three years. The Act does not say *within said three year period* or *prior to the end of said three year period,* but says *"At the end of three years."* In the present case the appellant was notified that the debtor was ready to pay into Court *prior* to the end of three years. The payment was not actually made, since it would have been foolish for the appellee to sacrifice his pigs in order to make this payment which the appellant had informed him would not be accepted.

The *Miller* case certainly does not hold, or purport to hold, that the debtor could not pay into Court the balance due unless he actually paid it *prior* to the end of the three years. The facts show the bankrupt notified the appellant *prior to the expiration of the period that he was refinanced* and was ready to pay into Court, but that without replying to appellee's letter of March 24, 1943, the appellant filed a petition for the sale of land and then notified the appellee that it would not accept the payment of the original appraisement even if it was made.

The appellee's petition for reappraisal is not for the purpose of delay or of denying the appellant any rights, but was for the purpose of insuring that the Court would either require the appellant to accept the balance due on the original appraisement, or the value set upon the property by such reappraisal. The evidence is that the appellee is willing to make either payment and is seeking merely to prevent the appellant from denying him the benefits of the Frazier-Lemke Act and depriving him of enhanced value of the property resulting from his three years' labor thereon.

The United States Supreme Court, in the case of *Wright v. Vinton Branch Mountain Trust Bank,* 300 U. S. 440, cited by appellant on pages 10 and 17 of its brief, passed upon the constitutionality of Section (s) and held that this section was constitutional, and that the Court did not have the right to grant more than a three year period of rehabilitation which could be terminated for cause at an earlier date. The Court

does not discuss a situation such as exists in the present case, and we see nothing in the dicta of this case that would affect the present case.

The case of *Wright v. Union Central Life Insurance Company,* 85 Law Edition, page 185, clearly shows the attitude of the United States Supreme Court as applied to a situation such as exists in the present case. The Court says:

> "The narrow issue presented by this petition for certiorari and which moved us to grant it is whether under Section 75 (s) (3) the debtor must be accorded an opportunity, on his request, to redeem the property at the reappraised value or at a value fixed by the court before the court may order a public sale."

In the present case the appellee is only asking that he be given an opportunity to redeem his property at the original appraised value, or at a reappraised value, or at a value fixed by the Court before the Court orders a public sale.

In the *Wright* case the Court also says, on page 187:

> "True, the granting of a request for a public sale is mandatory. But so is the granting of a request for a valuation at which the debtor may redeem. Yet a reconciliation of these seemingly inconsistent remedies is not difficult if the purpose and function of the Act are not obscured. This Act provided a procedure to effectuate a broad program of rehabilitation of distressed farmers faced with the disaster of forced sales and an oppressive burden of debt. * * * Safeguards were pro-

vided to protect the rights of secured creditors, throughout the proceedings, to the extent of the value of the property * * * There is no constitutional claim of the creditor to more than that. And so long as that right is protected the creditor certainly is in no position to insist that doubts or ambiguities in the Act be resolved in its favor and against the debtor. Rather, the Act must be liberally construed to give the debtor the full measure of the relief afforded by Congress (John Hancock Mut. L. Ins. Co. v. Bartels, supra; Kalb v. Feuerstein, 308 U. S. 433, 84 L. ed. 370, 60 S. Ct. 343, 41 Am. Bankr. Rep. (N. S.) 501, supra), lest its benefits be frittered away by narrow formalistic interpretations which disregard the spirit and the letter of the Act.

"Equal protection to debtor and creditor alike can be afforded only by holding that the debtor's request for redemption pursuant to the procedure prescribed in the first proviso of Section 75 (s) (3) cannot be defeated by a request of a secured creditor for a public sale under the second proviso. Certainly equal protection of debtor and creditor would not be obtained if the contrary view were followed. Then the debtor's rights under the first proviso would be either dependent on the outcome of his race of diligence with a creditor, for which customarily he would be poorly equipped (Cf. Kalb v. Feuerstein, supra); or they would be defeasible at the instance of a creditor. Under our construction, however, the debtor will be given the benefit of an express mandate of the Act. And the creditor will not be deprived of the assurance that the value of the property will be devoted to the payment of its claim. For, as indicated in Wright

v. Vinton Mountain Trust Bank, 300 U. S. 440, 468, 81 L. ed. 736, 746, 57 S. Ct. 556, 112 A. L. R. 1455, 33 Am. Bankr. Rep. (N. S.) 353, if the debtor did redeem pursuant to that procedure, he would not get the property at less than its actual value. In that case this Court, in sustaining the constitutionality of Section 75 (s), emphasized that the Act preserved the right of the mortgagee to realize upon the security by a judicial sale. By our construction the exercise of this right is merely deferred or postponed until the other conditions and requirements of the Act, prescribed for the protection of the debtor, have been met. It is eventually denied the creditor only in case he is paid the full amount of what he can constitutionally claim.

"* * * But there is nothing in that opinion or in the Act which says that that power of the court may be utilized so as to wipe out the clear and express right of the debtor under Section 75 (s) (3) to redeem at the reappraised value or at the value fixed by the court. Nor can the existence of that power be fairly implied. The power of the court to 'order the property sold or otherwise disposed of as provided for in this Act' cannot be taken to mean a discretionary power to terminate the proceedings through the exclusive device of a public sale. Congress has provided that certain contumacious conduct on the part of the debtor or his inability to refinance himself within three years may be an appropriate basis for a termination of the proceedings or for an acceleration thereof. We cannot infer, however, that Congress intended that such facts should have any further legal significance under the Act. To hold that they

empowered the court to deprive the debtor of his express and fundamental statutory right to redeem at the reappraised value or at the value fixed by the court would be to imply a power of forfeiture wholly incompatible with the broad design of the Act to aid and protect farmer-debtors who were victims of the general economic depression. * * * Such an important remedial right cannot be lost by mere implication. And to hold that the court has the discretion to deny or to grant the debtor's right to redeem at the reappraised value or at the value fixed by the court, dependent on general equitable considerations, would be to rewrite the Act, so as to vest in the court a power which Congress did not plainly delegate. This discretionary power of the court is exhausted when the court terminates the proceedings or accelerates their termination. Such termination can be effected only pursuant to the precise procedure which Congress has provided. And so we return to our reconciliation of the two apparently conflicting provisos of Section 75 (s) (3).

"We hold that the debtor's cross-petition should have been granted; that he was entitled to have the property reappraised or the value fixed at a hearing; that the value having been determined at a hearing in conformity with his request, he was then entitled to have a reasonable time, fixed by the court, in which to redeem at that value; and that if he did so redeem, the land should be turned over to him free and clear of encumbrances and his discharge granted. Only in case the debtor failed to redeem within a reasonable time would the court be authorized to order a public sale."

In the case of *In re Anderson,* 23 Federal Supplement 857, the Court, in commenting on the decision in this case of *Wright v. Mountain Trust Bank* cited by appellant, says:

> "In the language of the decision, 'Paragraph 3 also provides that "if * * * the debtor at any time * * * is unable to refinance himself within three years," the court may close the proceedings by selling the property. This clause must be interpreted as meaning that the court may terminate the stay if after a reasonable time it becomes evident that there is no reasonable hope that the debtor can rehabilitate himself within the three-year period.' But, for the farmer debtor to rehabilitate himself financially or refinance himself within the meaning of the provisions of subsection (s) of section 75, is it necessary that he place himself in position to pay in full all his creditors, secured or unsecured, or both? Or, is it only necessary that the debtor shall be able, during the statutory period of the moratorium, to pay a fair rental upon the property which he retains under subsection (s), both real and personal, with the exception of his unencumbered exemptions, and within such period put himself in position to pay for said property at its appraised, or, if reappraised, at its reappraised value? A careful reading of subsection (s) of section 75 in the light of the entire section shows, I think, that the latter meaning was intended.
>
> "It must not be forgotten that we are dealing with a bankruptcy law that has for its purpose the salvaging of farmers who are insolvent and unable to pay their debts in full."

The Court also, in commenting upon the right of the secured creditor to demand a public sale where the farmer is in a position to pay the original appraised value, says:

> "Pursuing this undoubted right, the secured creditor may deprive the farmer of the intended ultimate benefit of the provisions of the Act which is the saving of his farm. Yet I think it was in the mind of Congress that the ordinary secured creditor would usually be willing to accept, in lieu of his security, its fair cash value as established by a fair appraisal; that the farmer to refinance himself within the meaning of the Act should be compelled to refinance not his full indebtedness but only the appraised value of the encumbered property as well as the unencumbered property retained by him; that he should not be compelled, in any case, to refinance the entire secured indebtedness, if such indebtedness exceeds the value of its security except to the extent that he might have other property or assets available for that purpose. Otherwise, judging from observation and experience, section 75, subsection (s), intended to meet a great financial crisis among the farmers, can be helpful in comparatively few cases."

THREE YEAR MORATORIUM IS NOT A REDEMPTION STATUTE.

Appellant, in its brief, beginning on page 17, attempts to compare the three year moratorium or three year period of rehabilitation to a redemption period. This comparison is not supported by any authority

cited by appellant. Furthermore, it is clear that it is not a redemption period in the manner contended by the appellant. The Bankruptcy Act itself, Section 75 (s) (3), shows that even after the three year moratorium has expired and after the property has been advertised for sale and sold, *the redemption period starts.* The Act says that debtor shall have ninety days to redeem any property sold at such sale. If the debtor, during this ninety day period, fails to redeem, then he is forever foreclosed immediately from his property. The Bankruptcy Act, however, does not give any such effect to the three year moratorium. All that the three year moratorium provides is that if he fails to do certain things, the creditor may, at the expiration of three years, take certain legal steps, as a result of which he may start the running of a true redemption period.

The appellee does not see how any of the other cases cited by appellant apply specifically in the case at bar, to-wit:

In re Carter, 56 Fed. Supp. 385;
Corey v. Blake, 136 F. (2d) 162;
Hard v. Kirkpatrick, 91 F. (2d) 875;
Home Building and Loan Ass'n v. Blaisdell, 290 U. S. 398, 54 S. Ct. 231;
Stratton v. New, 51 S. Ct. 465.

CONCLUSIONS.

In view of the foregoing facts and decisions, the appellee contends:

1. That the appellee should be permitted to acquire his property free and clear of liens and encumbrances:

a. By payment of the original balance due on the original appraisal;

b. By payment of the balance due on a reappraised value if his present petition be granted; or

c. By payment of a sum fixed by the Court as being reasonable and representing the true value of the property, since, as stated by the United States Supreme Court in the case of *Wright v. Central Life Insurance Company,* 85 Law Edition, page 185:

> "* * * the debtor must be accorded an opportunity, on his request, to redeem the property at the reappraised value or at a value fixed by the court before the court may order a public sale."

2. That the case of *In re Miller,* 48 Supplement 13, is not controlling for the following reasons:

a. In that case the bankrupt had failed in every way to comply with the order of the Court during the period of moratorium, and the petitioner would have had a right to request a foreclosure even prior to the expiration of a moratorium period because of bankrupt's default; whereas in the present case the Conciliation Commissioner has found that the bankrupt complied in every respect with the order of the Court granting the moratorium, paid each year the rental value of the property as fixed by the Court, and the